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Jewelers' Vigilance Committee, Inc.

Memorandum submitted by the Jewelers'...

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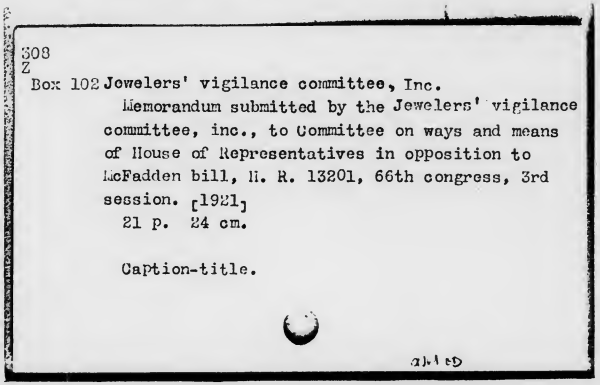

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Box 102 Jewelers' vigilance committee, Inc.
Memorandum submitted by the Jewelers' vigilance committee, inc., to Committee on ways and means of House of Representatives in opposition to McFadden bill, H. R. 13201, 66th congress, 3rd session. [1921]
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Prof. E. M. Borchard

MEMORANDUM SUBMITTED BY THE JEWELERS' VIGILANCE COMMITTEE, INC., TO COMMITTEE ON WAYS AND MEANS OF HOUSE OF REPRESENTATIVES IN OPPOSITION TO McFADDEN BILL, H. R. 13201, 66TH CONGRESS, 3RD SESSION.

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INTRODUCTION.

The purpose of the bill as stated in the title is:

> To provide for the protection of the monetary gold reserve by the maintenance of the normal gold production of the United States to satisfy the requirements of the arts and trades, by imposing an excise upon all gold used for other than monetary purposes, and the payment of a premium to the producers of newly mined gold, and providing penalties for the violation thereof.

This proposed legislation, if enacted, will operate in the following manner:

(1) A tax of approximately 50% will be levied on all gold used in manufacture or in the arts, irrespective of whether the gold taxed was mined during the current year or decades before.

(2) There will be paid over to every person or corporation producing newly mined gold from any mine within the United States, a subsidy equal to the sum of Ten Dollars, or approximately

Note: All page references are to pages in memorandum containing exhibits and submitted herewith.

50%, for every ounce of fine gold mined and delivered to the United States Mint.

In other words, this proposed legislation not only contemplates a subsidy to mine owners, but makes such subsidy conditioned upon a tax levy on certain arts and industries.

On June 1st, 1920, the Jewelers' Vigilance Committee, Inc., submitted to the Committee on Ways and Means a memorandum in opposition to the McFadden Bill. Our memorandum at that time included a statement of the Secretary of the Treasury condemning the McFadden Bill, and a well reasoned report of the Special Gold Committee appointed by the preceding Secretary of the Treasury, Mr. McAdoo, likewise opposing any artificial stimulation of gold production. Since that time there has been a change in general conditions which greatly affects the questions here involved and which, we believe, removes any justification whatsover for the passage of this Bill. Since then there have also been prepared certain other reports bearing on this situation, all disapproving the measure.

The American Bankers' Association appointed a committee of eminent bankers to examine into the merits of the McFadden Bill. This was composed of George M. Reynolds, Chairman, President of the Continental and Commercial National Bank of Chicago; Lawrence E. Sands, President of the First National Bank of Pittsburg, and A. Barton Hepburn, Chairman of the Advisory Board of the Chase National Bank, New York. These eminent bankers, being absolutely disinterested in any industry to be injuriously affected by the Bill, filed a unanimous report condemning the Bill, concluding with the statement: "It would

aggravate the very conditions which it seeks to remedy" (Page 75).

As a clear understanding of the McFadden Bill requires a consideration of certain basic underlying principles, the Jewelers' Vigilance Committee, Inc., has secured memoranda from two of America's leading economists. These are Professor E. R. A. Seligman, Ph. D. LL.D. of Columbia University, formerly President of the American Economic Association, and one of the best known economists in the country; and Professor E. W. Kemmerer, Ph. D. of Princeton University, a recognized expert on all economic matters, especially those relating to gold reserve, trend of prices and international economic situations. These gentlemen have considered this question independently, but have united in their thorough disapproval of the Bill.

A legal opinion as to the constitutionality of the proposed law is also included in the exhibits. This opinion cites numerous cases in which the courts have uniformly condemned a subsidy and clearly show that the proposed legislation is unconstitutional.

All the reports referred to, will be found in the exhibits submitted herewith for the convenience of your committee. We respectfully urge the careful consideration by your Committee of the reports contained in the exhibits which have been prepared by wholly disinterested persons, of unquestioned standing who uniformly condemn the Bill.

It is not our intention to elaborate in any way on the arguments presented by the eminent bankers, economists and mining engineers but we believe it will not be amiss to set forth briefly

some of the main points which we consider controlling and to refer to the opinions of the experts in reference thereto.

POINT I.

Any possible justification for the passage of the McFadden Bill at the time of its introduction has long since disappeared.

The proponents of this Bill seek to justify it on the ground that there has been a decreased output of gold in the United States and an increased use of gold in the arts.

At the outset, it must be borne in mind that the decreased output of gold was a direct result of the War. Scarcity and consequent high price of labor and of explosives and other materials used in gold mining were caused solely by war conditions. Likewise, the increased use of gold in industry was a direct result of the war. This is true in the first place because of the extravagance following the war and in the second place because of the rise in prices due to abnormal conditions. Rise in prices, in general, means that the value of commodities has increased in the terms of gold and that the value of gold has fallen in terms of commodities, and it therefore becomes comparatively cheap to purchase articles made of gold (pages 13, 67). It is quite apparent that a return to normal would have the affect of altering this condition and the facts prove that this is exactly what is happening now.

The figures which the proponents of the Bill were alarmed about in 1919 were that the output

for the year in the United States fell to $60,333,400. However, the gold market is an international one, and local production is an insignificant factor. The important question relates to the world's gold supply. This is what really affects the gold reserve. During the year 1920, the stock of gold in the United States was actually increased instead of decreased. In 1920, the exports of gold from the United States amounted to $322,100,000 and the imports amounted to $428,700,000. This shows a net gain of over $106,000,000 for the year 1920, which is almost double the industrial consumption of new gold in the United States during that period.

Likewise, the change in economic conditions is influencing the use of gold in the arts. This is natural and to be expected. The average monthly withdrawals from the Assay Office in New York gives us the key to this situation. The withdrawals from the New York office represent approximately 85% of the Nation's withdrawals and show that during the *last* three months of 1920 the withdrawals were 43.8% less than the average monthly withdrawals during the *first* three months of the same year. This is true despite the fact that the industrial consumption of gold is usually much greater during the last quarter because of demands of the holiday seasons, etc.

Moreover, it is quite apparent that this situation is rapidly regulating itself at an even greater rate than these figures indicate. The fall in prices of commodities during the year has been tremendous and this fall in prices, including wages, is progressing even more rapidly (Page 45).

We have here a practical illustration of the automatic regulator which is constantly at work in fixing the supply of gold. This is discussed at length in the memoranda of Professors Seligman and Kemmerer. This condition was recognized by the British Treasury Committee and its report in 1919 emphatically registered its disapproval of any legislative interference with the production of gold.

The report submitted to the Secretary of the Treasury by the Special Gold Committee appointed by him, said:—

> "The cessation of hostilities has radically changed this situation, and, with the change in the situation, any need of particular effort to promote or stimulate our gold production which may have existed has ceased. There is now no danger of an impairment of confidence" (Page 6).

It then pointed out that normal conditions would soon follow saying:

> "Under these circumstances, there is in our opinion no need for artificial stimulation of gold production. Not only has any need therefor passed, but there have come into operation causes that will in due time restore all industry, including the mining of gold, to a normal basis. Gold mining will then become again normally profitable and respond automatically to normal stimuli" (Page 7).

Present conditions have taken just this course and now even a leading representative of the gold miners realizes this. Mr. H. L. Slosson, of Nevada, who is prominent in mining affairs and President of the Middle Mines Association, and a

member of the American Institute of Mining and Metallurgical Engineers, is quoted as saying:

> "I do not expect the McFadden Bill to pass Congress. It is generally opposed by the banking interests, from one end of the country to the other, and their opposition would be sufficient, even though the farmers and manufacturers did not join them.
>
> The fact is not so important as it might seem to the gold mining industry.
>
> The most important and outstanding fact is that gold rapidly is rising in value all over the world, for it is an axiom of political economy that as prices fall, gold rises; and as prices rise, gold falls.
>
> The last few years have been crucial for the gold producer, but the tide has turned with a rush and the gold miner is coming into his own."

The industrial use of gold is rapidly decreasing to the pre war level, the cost of production, including labor and commodities, is declining and the difficulties pictured by the mining interests have disappeared to a great extent. Before long gold mining will again be restored to its former enviable position of substantial profits with an unlimited and constant market.

POINT II.

The McFadden Bill attempts to protect the gold reserve "by the maintenance of the normal gold production in the United States." This overlooks the fundamental principle that the maintenance of a national gold reserve depends upon international, not national, factors.

The gold reserve of a single nation must be considered from an international point of view. It is self evident that the gold supply of the world is the result of the accumulation of the gold production of the past ages. The very fact that gold is durable is the reason for its use as the monetary basis.

The statements made by the proponents of this measure that gold is consumed, are clearly overstatements, for although gold is used in the arts, only a negligible percentage is ever destroyed or consumed and much of the gold in the market today was produced before the Christian Era. It is impossible therefore to conceive of any line of reasoning which would substantiate the statement made by the gold mining interests that the gold reserve is vanishing. The stock of monetary gold in the principal countries of the world as estimated by the United States Director of the Mint, (Page 41), for the years 1913, the last year before the war, was in excess of 8 billion dollars. The estimated gold production of the world for that year (the third largest production of any year in history up to that time) was approximately 450

million dollars or less than 6% of the total stock of monetary gold in these countries. For the year 1919 the world production of gold as estimated by the Director of the Mint, was less than 5% of the total world gold stock. Naturally every year the annual production must represent a smaller percentage of the accumulated stock than it did the year preceding. The production of new gold in the United States, at its height was less than 1% of the total world's supply (Page 53). The gold used in the arts in this country in the year 1919 amounted to less than 1% of this country's gold reserves. This infinitesimal drain cannot be considered as having any importance whatsoever.

The market for gold is a world market, as gold is the money of international trade. With it trade balances are settled and the shipment of gold from one country to another for that purpose has a far more direct and appreciable effect on an individual nation's gold supply than either the national production of new gold or the national use of gold by the arts and industries. In this connection, it is interesting to note that the imports of gold to the United States for the year 1920 as previously pointed out, exceeded the exports of gold from the United States by a sum in excess of 106 million dollars. In other words, the increase in our gold supply through excess of imports over exports was greater than the annual production of gold in this country in any single year.

As a matter of fact this nation today holds approximately 36% of the entire gold supply of the world. The relation of domestic production of new gold, and domestic use of gold by the arts, to the total world supply of gold shows how in-

significant would be either an artificial stimulation of gold production or an artificial reduction of use of gold in the arts. Even assuming that the McFadden Bill would accomplish an increase in the domestic production of new gold, it is evident that the measure as proposed would be placing this Government in the position of paying a bounty for the benefit of the rest of the nations of the world, and would make the United States assume the burden of the entire world.

The report of the Committee of the American Bankers Associations, points out (Page 67)) :

> "If at any time the banking situation calls for more gold in the United States, we can purchase it in the international gold markets far more cheaply than we can obtain it by the doubtful method of an expensive bonus on new gold produced in the United States, which could at best make a difference of only two or three tens or millions per annum."

Moreover, it must be remembered that with the gold standard, there is an automatic regulator at world. The rise of prices of recent years was primarily due to the abnormal conditions of the war. Over long periods of time, however, fluctuations in price levels are due directly to relative alterations in the supply of gold. In proportion as prices rise, gold mining becomes unprofitable and there is a natural relative falling off in the production of new gold. With this dropping off in the supply, prices begin to fall and as prices recede, gold mining becoming more profitable and production of gold increases, as a result of this automatic regulator. This is clearly protrayed in the lucid statements of Professors Kemmerer and Seligman. We furthermore urge an examination of the charts contained in the exhibits submitted herewith.

This automatic regulator has already commenced to work (See Point I). Falling prices translated into costs of production, have led to the stimulation of gold production. Artificial interference with world-wide economic forces, is tremendously dangerous. The problem should be allowed to adjust itself by natural causes. The maintenances of the gold standard depends upon the absence of legislative interferences.

POINT III.

If the McFadden Bill becomes law it will
(a) Debase the gold standard;
(b) Create an indefinite, increasing drain on the United States Treasury;
(c) Invite fraud on a tremendous scale; and,
(d) Encourage the wasteful dissipation of the nation's supply of gold ore.

The very first requisite of the maintenance of the gold standard is that there must be no interference with its supply. "Any artificial inducements to increase the quantity of gold will pro tanto endanger its use as a standard" (Page 26). A subsidy would interfere with the maintenance of the free gold market, which up to the outbreak of this war was the pride of all the leading commercial countries. The regrettable departure of some nations from the gold standard through the necessities of the late war should not be followed as an example by this nation. The United States

has acquired an enviable position since the war and is on the way to becoming the world's financial centre. The financial structure, however, is so sensative, that the least interference with it is apt to alter the entire situation. The grant of a subsidy to gold mines would show doubt on our Government's part as to its ability to maintain the gold standard and would arose suspicion in foreign markets. This would abruptly terminate the development which is now rapidly proceeding and the possibility of the United States becoming the international monetary centre (Page 32).

In the opinion of the Committee of the American Bankers Association, this danger to the maintenance of the gold standard is the greatest objection to the Bill (Page 72). It states that at present the world regards our dollars as good as gold and that our offer to pay a premium for the production of gold would raise a doubt as to their value. It therefore states that

> "Action of the kind proposed by the United States would be a red flag to the commercial world. The passage of the McFadden Bill, instead of strengthening confidence in the position of the United tSates, would weaken it; it would be considered a confession of weakness. The McFadden Bill should be opposed by every wellwisher of this country's credit and commercial and financial prosperity" (Page 73).

As further stated by Professor Kemmerer in his memorandum (Page 57):

> "Creditors having contracts payable in gold may perhaps reasonably be expected to have assumed the risks of the fluctuations, that should take place during the period of their contracts, in the value of gold from natural causes, but they may not be reasonably expected to have assumed losses resulting from legislation deliberately planned to push down or hold down the value of gold."

The McFadden Bill provides that the bounties to the gold mining companies would have to be paid even if the tax received from the users of gold would be insufficient to meet the amount of the bounty. If the bill were to accomplish its purpose a two-fold effect would result. The amount of new gold mined would be increased and the amount of gold used in the arts would be decreased. In terms of Government revenue and disbursement this would mean that the subsidy paid to the gold mining corporations would increase while the revenue received from the arts and industries using gold would decrease. The difference between this income and disbursement would have to come from the general Treasury. It is, of course, impossible to ascertain in advance the amount to which the Government would be committing itself through the enactment of any such measure. Aside from the fact that this amount would annually reach a substantial figure far in the millions,—its very indefinitness raises a real criticism. The figures for 1918 clearly show that under this Bill the Government would have been compelled to raise through general taxes, over and above the special tax to be levied upon the users of gold, a sum in excess of 32 millions of dollars in order to pay (to the gold miners) the contemplated bounty. (Page 61). Only if all of the new gold annually produced is used in the arts, would there be no drain on the general Treasury of the United States. In so far, as this

legislation would increase the production of new gold, and decrease the use of gold in the arts, would it be necessary to pay the bonus created by such differences from the general Treasury.

In so far as the payment of a subsidy to gold mining corporations is an inducement to accomplish increased production, just so great would there be a corresponding inducement to establish fraudulent claims for the substantial bounty to be paid by the Government. A bounty which would make new gold worth $30.67 an ounce in the hands of the producer, while old gold is only worth $20.67 an ounce, would be a powerful stimulus to fraud. Fraudulent practices to this end would be easily carried on and extremely difficult to detect. The individual prospector would promptly see the advantage in "mining the bounty." And "mining the bounty" would become an important American industry. (Page 58.)

The twenty dollar gold piece would be worth approximately thirty dollars if fraudulently put through as new gold. If it were conceivable that a plan could be devised to distinguish new gold from old gold, there would be a faint hope of preventing fraudulent claims for the bounty. A fifty per cent. profit is substantial and most inviting for "salting" gold ores with gold pieces.

The bounty as contemplated would doubtless yield enormous profits to the most productive mines, many of which are still on a good paying basis.

It would naturally encourage all producers to work their richest ores as long as the bounty would last and to neglect the poorer mines and the inferior ores in the better mines. The purpose of the bounty no doubt was to encourage the working of the poorer mines and the poorer ores in the better mines. This result would not be accomplished, as gold producers would realize that the life of the bounty would be uncertain. On this subject the British Gold Production Committee said in its report of 1918:

> "It appears to us that anything in the nature of a subsidy per ounce produced * * * would be an inducement to a mine to work the better ore * * *." (Page 56.)

In no surer way could this nation encourage the wasteful use of its gold ore than through the creation of the proposed bounty.

POINT IV.

The producers of new gold are not entitled to a bounty.

The only possible justification for payment of a bounty is that the industry to be benefited is charged with a public purpose.

It is obvious, of course, that the fostering of every industry would react to a public benefit, but it is not this indirect public benefit that justifies payment of public funds to private industry. To support such payment it is essential to show that it is necessary for the public welfare that the industry in question be subsidized.

No overwhelming public necessity requires such payment to the gold miners any more than to producers of copper or iron, or other industries essential to the welfare of the nation.

The British Report of 1918 emphatically declared that there was no justification for such a bounty being paid from public funds to the gold mining industry. (Page 23.)

The American Bankers Association Committee likewise recognized that no national emergency existed for the separate treatment of the gold mining industry to justify the Government's singling it out for its benefactions.

Even assuming that there were a public necessity, there would be no justification for invoking the novel principle of compelling specially selected industries to pay taxes which are to be turned over as a bounty or subsidy to the gold mining interests. This is particularly apparent when it is realized that in many instances the payment of the bounty to the gold mining companies, now operating at a profit, would be nothing less than an outright gift.

Furthermore, it is interesting to note that the proponents of this measure have failed to demonstrate to your Committee the fact that in periods of deflated prices and lower costs of production large profits were made by gold mining companies. No industry holds the advantage necessarily possessed by gold miners, in that the unlimited production of gold finds an immediate market at a fixed price without any selling expense. A cursory investigation will show to your Committee that even at this time some gold mining corporations are declaring dividends, and we cannot fail to comment upon the fact that the proponents of this measure have never presented figures which could lead to any scientific consideration of the present costs of production and the relationship of same to the decrease of

output. To allow a bounty to the gold mining companies would be extending an invitation to every industry of the nation to appeal for relief as soon as the normal profits of such industry in any way declined.

Legislation of this type is naturally fraught with the danger of encouraging an assault by all equally deserving industries upon the coffers of the Treasury of the United States.

POINT V.

The McFadden bill is unconstitutional.

This bill proposes to grant a subsidy to certain industries, to be paid for by monies collected from other industries.

At the first hearing of the Committee on Ways and Means to consider this bill, held on May 25, 1920, the proposer of the bill explained its purpose. After the explanation as to the bounty, the following colloquy appears in the minutes, page 8:

> "Mr. Garner: And you propose to do that under the taxing clause of the constitution?
> Mr. McFadden: Yes.
> Mr. Garner: Well, I did not know you used the taxing clause of the Constitution for the purpose of promoting a business. Of course, it has always been our idea to use the taxing clause of the Constitution to get revenue in the Treasury and not for the purpose of either depressing or promoting any enterprise or business."

The question raised by the member of your Committee touches the vital underlying constitu-

tional objection to this bill. We have here the unheard of proposition of using the taxing clause of the Constitution for enriching an individual industry. The decisions of the United States Supreme Court are unanimous in condemning any such use of the taxing power. The payment of monies as a subsidy to gold mining corporations would be clearly unconstitutional even if the monies so paid were to come from the general Treasury of the United States. The Supreme Court of the United States in unequivocal terms has condemned similar legislation.

This measure, however, contemplates a novel departure from the ordinary uses of the taxing power of Congress. To quote from the decision of the United States Supreme Court in the case of *Loan Association* vs. *Topeka,* 20 Wallace, 655, page 664:

> "To lay with one hand the power of the Government on the property of the citizen, and with the other to bestow it upon favored individuals to aid private enterprise and build up private fortunes, is none the less robbery because it is done under the forms of law and is called taxation. This is not legislation. It is a decree under legislative forms."

Any attempt to tax one part of the community for the purpose of obtaining funds, not for the public treasury, but for another group of the community, is abhorrent to our ideas of taxation. The proposed subsidy violates all the fundamental principles of taxation and is clearly unconstitutional and un-American. (Pages 76-84.)

POINT VI.

The leading financial and economic authorities, official and otherwise, throughout the world, are opposed to any plan of artificial stimulation of gold production.

This question was first officially considered by the Gold Production Committee apointed by the Commissioners of the British Treasury, which reported under date of November 29, 1918 against subsidizing the gold industry.

This report received the approval of the Committee appointed by the Secretary of the Treasury of the United States, which Committee reported under date of February 11, 1919. This Committee consisted of Hon. Albert Strauss, a member of the Federal Reserve Board, Hon. Raymond T. Baker, Secretary of the Mint, Hon. Emmett D. Boyle, Governor of the State of Nevada, Hon. Edwin F. Gay, well-known economist and Pope Yateman, Esq., one of the leading mining engineers of the United States. This committee conferred with Professor Irving Fisher, and other eminent economists and examined a vast amount of data submitted by representatives of gold mining corporations. The committee was unanimous in its condemnation of any artificial stimulation of gold production and expressed gratification at the unaminity of opinion against such measures (Page 8).

The present Secretary of the Treasury of the United States, Hon. D. F. Houston, under date of April 9, 1920, addressed a letter to Hon. Joseph

W. Fordney, Chairman of the Committee on Ways and Means of the House of Representatives, specifically referring to the McFadden Bill now under consideration, and flatly stated that.

> "The Treasury is very much opposed to this bill." (Page 9).

This condemnation of the McFadden Bill is repeated in the last annual report of the Treasury, which report covered the fiscal year ending June 30, 1920. (Page 10).

Professor E. W. Kemmerer is vigorous in his denunciation of the measure, pointing out its inherfent defects. (Pages 34-64). Professor E. R. A. Seligman likewise condemns the measure, concluding his treatise with the statement

> "It would be deplorable in the extreme if Congress were to be misled by the specious arguments of those who have everything to gain and nothing to lose into accepting a proposition the condemnation of which by impartial and unprejudiced authorities has been so pronounced and so unanimous." (Pages 11-34).

The special committee appointed by the American Bankers Association to consider the McFadden Bill is also unanimous in its condemnation of the measure. The names of the members of this committee are mentioned elsewhere, and the members of this committee represent the sound financial and banking opinion of the nation. (Pages 64-75).

Various members of the Ways and Means Committee at previous meetings mentioned the doubtful constitutionality of the proposed bill. An opinion of the Counsel to the Jewelers Vigilance

Committee, Inc., is likewise submitted for your consideration. This opinion of Counsel, citing various decision of the United States Supreme Court clearly establishes the unconstitutionality of the proposed bill. (Pages 76-84).

All of the official and experts above mentioned base their opposition to the McFadden Bill on broad principles of national and international public policy.

Their opinions are impartial, represent various angles of approach, and in no way are colored by any special plea for relief, or any special requests for private benefits. Their objections are directed against fundamentals and cannot possibly be circumvented by any structural changes in the bill.

CONCLUSION.

After considering the reports and arguments presented, it is confidently urged that your Committee can come to but one conclusion, namely, that this measure is unconstitutional, unnecessary, economically unsound, and would be positively injurious to the best interests of the country. It must therefore be disapproved.

Respectfully submitted,

JEWELERS' VIGILANCE COMMITTEE, INC.,
Sub-committee on Gold.
G. H. Niemeyer, Chairman,
Harry C. Larter,
John W. Sherwood.

February 8, 1921.

GREENBAUM, WOLFF & ERNST,
Of Counsel.

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